

B8595E

3.R36

1988/89

Copy 1

REPORT OF REVENUE OUTLOOK FOR
LAST SIX MONTHS OF FY...

B8595E
3. R36
1988/89
Copy 1



STATE OF SOUTH CAROLINA
BOARD OF ECONOMIC ADVISORS

Walter R. Pettiss, Chairman
Andrew J. Crane
Thomas E. Snider, Ph.D.
S. Hunter Howard, Jr., Ex officio
Barbara A. Feinn, Ph.D., Executive Director

Rembert C. Dennis Building
Suite 440
1000 Assembly Street
Columbia, S. C. 29201
803/734-3784

To: South Carolina Budget and Control Board
Subject: Report of Revenue Outlook for Last Six Months
of FY 1988-89

S. C. STATE LIBRARY
JAN 11 1989
STATE DOCUMENTS

The Board of Economic Advisors is required by Section 11-9-880 of the 1976 South Carolina Code of Laws to provide a synopsis of the revenue outlook for the last six months of the fiscal year on December 31st of each year. The synopsis for December 31, 1988 is provided herein with supporting tables.

The economic situation and outlook since the November 1 forecast continue with as much uncertainty as before. There is one less unknown with the election of Vice President Bush, but his policy decisions in confronting the budget and trade deficits and their impact on economic trends are yet to be determined. The national economic forecasters differ on the meaning and repercussions of the deficit on the outlook for the economy. There is also wide divergence of views on the impact of the various policy choices before the President-elect.

The deficits and their solutions are of a longer term nature although the financial markets tend to treat them as of short term consequence. Significantly more is involved than fine-tuning of monetary and fiscal policy to arrive at solutions for the short term. The future of the U. S.

as a viable first rate economic power is the real major issue for concern. In the intermediate period looms the extent of the deterioration from damages to the U. S. position until necessary steps are taken to insure America's long term competitiveness.

The short term consequences of the deficits are seen mainly as changes in cyclical sightings and forecasts. The longer term secular changes and the future fundamental role of the U. S. economy on the world scene are submerged by immediate movements and trends which have been favorable and essentially as projected. Gains in personal income are within the 6.5% to 7.5% range. Real growth has been moderate but positive. Unemployment nationally hovers at rates just above and below 5.5%, while in South Carolina unemployment rates are lower, remaining below 5% since February and dipping to 4.4% in July. Inflation and interest rates have been moving upward as anticipated.

Revenues generated for the first six months of the fiscal year are reflecting a favorable economy in South Carolina at the present time. Employment and income growth which had been faltering seem to have revived. There is, however, concern for the future course of the national and international economies in which the South Carolina economy operates. The repercussions from a faltering U. S. economy will clearly impact on South Carolina even with an economy in the State that has the appearance from revenue collections at this time of strength and vigor.

Given the uncertainty at the national level and with no new clear data to serve as the basis for change, the economic forecast of November 1 would seem the most probable scenario. The outlook for the estimate was one of continued but uneven expansion but with a real danger of a downturn of either the soft landing or boom/bust variety occurring sometime during the

period through June 1990, with the second quarter of 1989 targeted as the most likely initial quarter of the four-quarter slowdown. This encompasses the next six months. These are consensus forecasts.

Estimates of revenue collections from December 1988 through June 1989 will be influenced by the uncertainty at the national and international level, as well as by the strength in Christmas sales and fluctuations in the general economic outlook at the State level. With this as background, even with revenues for the current fiscal year seeming to be stronger than anticipated, the Board of Economic Advisors has elected to wait until the February 15 review to determine whether a change in the revenue estimate is warranted.

On February 15, with two more months of revenue collections and a clearer indication of the direction of the economy in the first quarter, a better assessment of the underlying strength of revenue collections should be possible.

Board of Economic Advisors

W.R.P.

December 31, 1988

TABLE I

GENERAL FUND REVENUES
Forecast 1988-89 and 1989-90
In Millions of Dollars

	ACTUAL 1987-88	ESTIMATE 1988-89	ESTIMATE 1989-90
TOTAL GENERAL FUND (1)	2938.4	3102.7	3280.0
Total Regular Sources (1)	2887.3	3058.0	3238.0
Sales Tax (1)	1006.2	1075.0	1119.0
Individual Income Tax	1142.2	1233.0	1329.0
Corporation Income Tax	196.2	206.0	219.0
All Other	542.7	544.0	571.0
Miscellaneous Sources	51.1	44.7	42.0
Education Improvement Fund	251.1	268.75*	279.65*
Interest on Education Improvement Fund	1.7	1.9	1.9
TOTAL	252.8	270.65	281.55
	<u>RATES OF CHANGE**</u>		
TOTAL GENERAL FUND		5.6%	5.7%
Total Regular Sources		5.9	5.9
Sales Tax		6.8	4.1
Individual Income Tax		8.0	7.8
Corporation Income Tax		5.0	6.3
All Other		0.2	5.0
Miscellaneous Sources		-12.4	-6.0
Education Improvement Fund		7.0	4.1
Interest on Education Improvement Fund		13.1	-
TOTAL		7.1	4.0

(1) Net of Education Improvement Fund.

* One-fifth of total sales tax.

** Percent change based on unrounded figures.

NOTE: FY 1987-88 historical data and corresponding percent changes adjusted in accordance with Comptroller General's modifications under GAAP procedures as of December 12, 1988.

TABLE II

REVIEW OF GENERAL FUND REVENUE COLLECTIONS AND STATE INCOME GROWTH

FISCAL YEARS	PERSONAL INCOME AT ANNUAL RATES (MILLIONS OF \$)	PERCENT CHANGE PRIOR YEAR QUARTER	CUMULATIVE GENERAL FUND REVENUE (MILLIONS OF \$)	PERCENT CHANGE PRIOR YEAR QUARTER	RATIO OF REVENUE GROWTH TO INCOME GROWTH

1985-86					
1985: 3	35,932	6.45	631.355	2.46	0.381
4	36,667	7.03	1254.505	3.14	0.446
1986: 1	37,430	6.70	1842.936	2.92	0.435
2	37,906	6.90	2509.288	4.84	0.701
1986-87					
1986: 3	38,350	6.72	665.543	5.42	0.805
4	38,961	6.25	1364.079	8.73	1.396
1987: 1	39,738	6.16	1990.810	8.02	1.301
2	40,647	7.23	2692.754	7.31	1.011
1987-88					
1987: 3	41,413	7.98	726.531	9.16	1.147
4	42,641	9.44	1472.082	7.92	0.838
1988: 1	42,923	8.01	2127.654	6.87	0.858
2	43,840	7.85	2938.379	9.12	1.161
1988-89					
1988: 3	44,500 *	7.45	781.428	7.56	1.014
4	45,550 *	6.82	1555.600 *	5.67	0.832
1989: 1	46,162 *	7.54	2281.600 *	7.24	0.959
2	46,587 *	6.26	3102.700 *	5.59	0.892

*: Forecasts, Board of Economic Advisors, October 25, 1988.

Note: FY 1987-88 historical data and corresponding percent change and ratio adjusted in accordance with Comptroller General's modifications under GAAP procedures as of December 12, 1988.

Board of Economic Advisors
December 31, 1988

REVENUE FORECASTING PROCEDURES
BOARD OF ECONOMIC ADVISORS
FISCAL YEARS 1989 AND 1990

The procedures and methodology of the Board of Economic Advisors in the preparation of the revenue forecasts for Fiscal Years 1988-89 and 1989-90 as of December 31, 1988 and January 1, 1989 involved three major stages beginning with preparation of the November 1 first official forecast for FY 1989-90: 1) providing the economic background and setting at the national and State levels for the revenue forecasts; 2) interpreting recent and historical revenue relationships; and 3) interacting with officials of other states with responsibility for revenue forecasting.

The Board members had meetings as in the past with experts and professional economists for economic intelligence gathering. These included a meeting in Columbia on October 19, 1988 with David A. Wyss, Ph.D., Senior Vice President and Financial Economist, Data Resources, Inc.; Dan M. Bechter, Ph.D., Vice President, Federal Reserve Bank of Richmond; Ben E. Laden, Ph.D., Economist and Partner, Maryland Capital Management, Inc.; Bruce L. Williams, Corporate Economist, Southern Bell Telephone Company, Atlanta; Bruce Yandle, Ph.D., Alumni Professor of Economics, Department of Economics, Clemson University; Ronald P. Wilder, Ph.D., Chairman, Department of Economics, University of South Carolina; and James A. Morris, Ph.D., Distinguished Professor of Economics Emeritus, University of South Carolina, in which the outlook for the economy of the nation and South Carolina was discussed. The resources of the national forecasting groups by which the SCOPE model, when operative, and other forecasts are driven, Data Resources, Inc., Evans Economics, Inc., and WEFA, Inc., were available weekly and monthly to Board members and staff. Materials from a variety of sources--international, national and State publications--were also made available to Board members and staff. In addition, there was Board interaction with Martin S. Feldstein, Professor of Economics, Harvard University and President of the National Bureau of Economic Research, and former Chairman of the President's Council of Economic Advisors, and Roger E. Brinner, Chief Economist, McGraw Hill Financial Services Company, and others at the U.S. Economic Outlook Conference held on October 4 in New York City by Data Resources, Inc. Additionally, there was Board interaction with Lawrence Chimerine, Chairman, the WEFA Group; Mark Zandi, Director, U.S. Financial Services; Paul Getman, Director, Financial Services Group; and others of WEFA at regional conferences held on September 22 in Atlanta and on December 1 in Washington, D.C. by the WEFA group, as well as Board participation at the Federation of Tax Administrators Annual Conference on Revenue Estimating October 16-19 in Chicago.

On October 19 the newly constituted Board of Economic Advisors convened in preparation for the first official estimate for FY 1989-90. The Board considered several approximations for FY 1989-90 based on information received from visiting economic and financial experts as well as on revenue collections and further economic and revenue analysis. Board members decided on December 8 to forego a meeting tentatively scheduled for December 15 since it was determined that there was no basis for change in the estimates.

BRIEF OVERVIEW OF THE SCOPE MODEL

The SCOPE (South Carolina Operations Planning and Evaluation) Model was initiated in 1972 in the Office of Chief Economist (originally in the Governor's office). It was designed and operated as a policy and forecasting tool for top level executive, legislative and management decision making. SCOPE is an econometric model designed to reflect the South Carolina economy and to forecast the performance of major economic variables in the State, particularly tax revenues, employment and income. The model is based on a framework of economic activity in the State relative to national economic activity with approximately 85 exogenous national variables provided by leading national forecasting services such as Data Resources, Inc., the WEFA Group, and Evans Economics, Inc.

The SCOPE core model consists of 63 equations, of which 55 are stochastic* and 8 are identities. SCOPE attempts to reflect the diversity of the South Carolina economy by including 20 industrial sectors of manufacturing and nonmanufacturing employment, and a series of equations for wages, personal income, unemployment, taxable sales and State tax revenue.

Durable Manufacturing Employment

The durable manufacturing employment block consists of 6 stochastic equations for the major industries in the State as reported by the South Carolina Employment Security Commission. The employment equations for each separate industry are expressed as a function of a national consumption expenditure index appropriate for that particular industry, a national industrial production index corresponding to that industry and the national level of employment in that industry. The durable employment forecasts include the following industries: Lumber and Products, Stone, Clay and Glass, Fabricated Metal Products, Electrical and Nonelectrical Machinery, and Other Durables which includes Furniture and Fixtures, Instruments and Related Products.

Nondurable Manufacturing Employment

The nondurable manufacturing employment block consists of 7 stochastic equations for the major nondurable industries in the State. Like the durable block, the employment equation for each industry is expressed as a function of a national consumption index appropriate for that particular industry, a national industrial production index for that particular industry and the national level of employment in that industry. Employment forecasts are available for each of the following nondurable industries: Food and Kindred Products, Textile Mill Products, Apparel, Paper, Printing and Publishing, Chemicals, and Other Nondurables, such as Rubber and Miscellaneous Plastics Products.

Nonmanufacturing Employment

The nonmanufacturing employment block is disaggregated into 7 stochastic equations: Construction, Transportation and Public Utilities, Services, Trade, Finance-Insurance-Real Estate, State and Local Government, and Federal Government. Employment growth in these industries is specified as functions of State population, national employment in these industries and national consumption indices.

Personal Income

The personal income block is composed of 11 equations, one equation for the unemployment rate, and 10 additional equations for each of the 10 major components of personal income as published by the Bureau of Economic Analysis, Department of Commerce. These equations are specified as functions of their respective national and State income and employment variables. In addition, equations are estimated for wage and salary disbursements for all major industries and are specified as functions of national wage trends and State employment levels.

Revenues

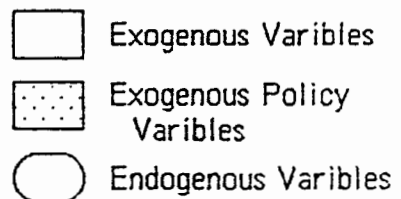
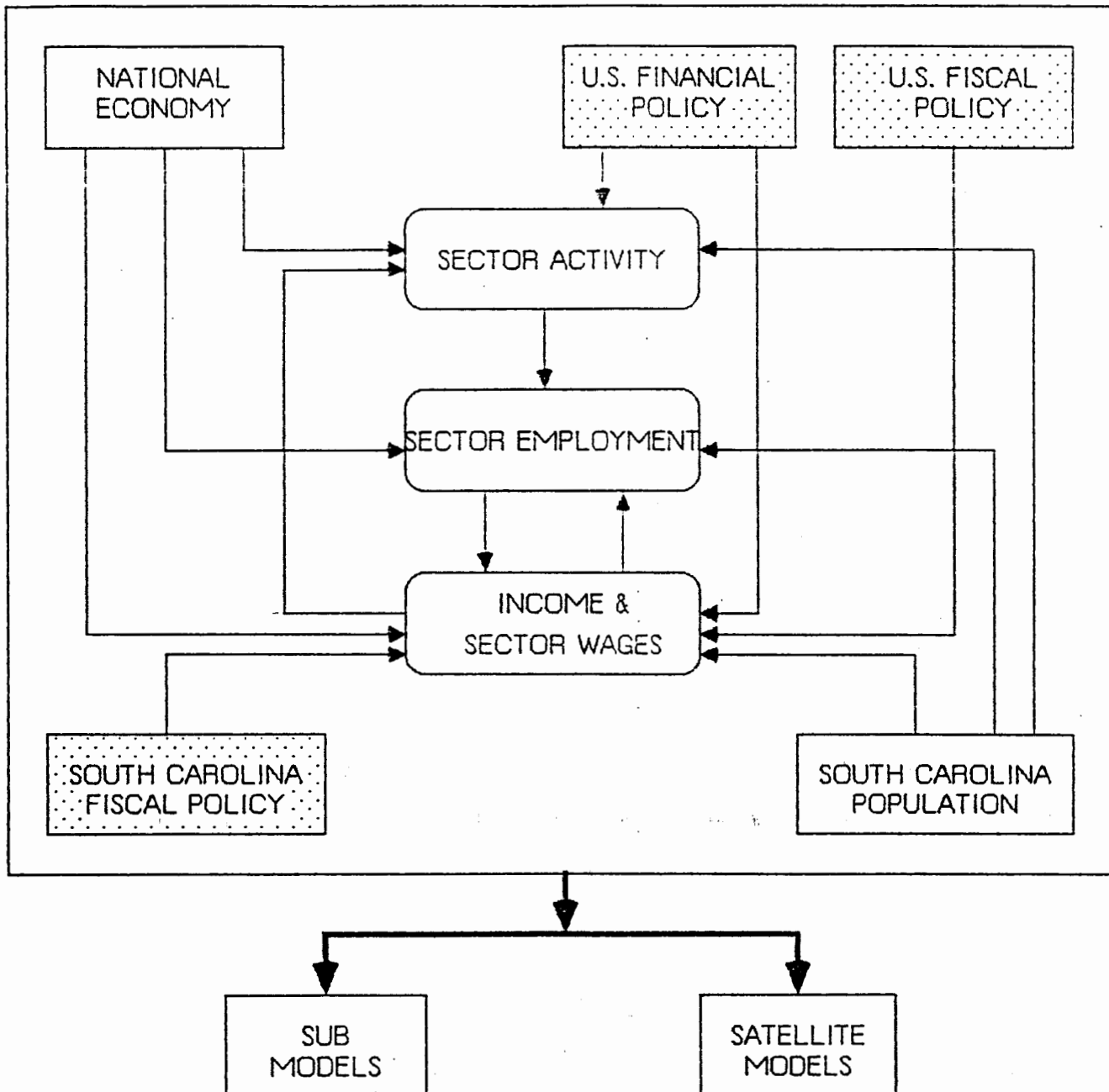
The revenue section of the model emphasizes 4 major stochastic Regular Revenue Sources equations: 1) South Carolina corporate income tax, 2) South Carolina individual income taxes, 3) South Carolina retail sales tax, and 4) all other taxes. These equations are individually specified as functions of aggregate employment and income with their respective coefficients and constants. In addition, there are 2 stochastic equations for taxable sales and refunds.

The model is currently undergoing major revisions to incorporate recently developed econometric techniques and to reflect significant structural changes in the national and South Carolina economies.

Board of Economic Advisors
December 31, 1988

SCOPE MODEL

SOUTH CAROLINA OPERATIONS, PLANNING & EVALUATION MODEL





STATE OF SOUTH CAROLINA
BOARD OF ECONOMIC ADVISORS

Walter R. Pettiss, Chairman
Andrew J. Crane
Thomas E. Snider, Ph.D.
S. Hunter Howard, Jr., Ex officio
Barbara A. Feinn, Ph.D., Executive Director

Rembert C. Dennis Building
Suite 440
1000 Assembly Street
Columbia, S. C. 29201
803/734-3784

REVENUE OUTLOOK - FY 1989-90

AS OF JANUARY 1, 1989

The Board of Economic Advisors is required by Section 11-9-880 of the 1976 South Carolina Code of Laws to consider adjustments to the official revenue forecast for the 1989-90 fiscal year on January 1, 1989. It has done so. It determined that while forecasts for FY 1989-90 revenues stand to some extent on their own, they are also influenced by the level of anticipated collections of FY 1988-89. Therefore, no adjustment in the forecast of \$3280 million made on November 1, 1988 is warranted until December and January revenue data are available and a clearer indication of the direction of the economy in the first quarter of 1989 emerges.

Board of Economic Advisors

W.R.P.

January 1, 1989

TABLE III

TOTAL GENERAL FUND REVENUES
 QUARTERLY ESTIMATES
 Fiscal Years 1988-89 and 1989-90
 (In Millions of Dollars)

	FY 1988-89 -----	FY 1989-90 -----
FIRST QUARTER	770.6	816.7
SECOND QUARTER	1555.6	1653.1
THIRD QUARTER	2281.6	2407.5
FOURTH QUARTER	3102.7	3280.0

PERCENT OF TOTAL REVENUES
 COLLECTION BY QUARTER

	FY 1988-89 -----	FY 1989-90 -----
FIRST QUARTER	24.8	24.9
SECOND QUARTER	25.3	25.5
THIRD QUARTER	23.4	23.0
FOURTH QUARTER	26.5	26.6

Board of Economic Advisors
 October 25, 1988

NOTICE

Pursuant to Section 11-25-690 of the S.C. Code of Laws, 1976 and amended, a request must be received in writing at least ten days prior to February 10, 1989 to continue to receive the publications of the Board of Economic Advisors. If such a written request is not received by February 1, 1989, in compliance with Section 11-25-690 of the S.C. Code of Laws, 1976 and amended, your name will be removed from the Board of Economic Advisors mailing list.

Board of Economic Advisors
January 1, 1989